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No. 81-993

IN THE

Supreme Court of the United States

October Term, 1981

CALIFORNIA FEDERAL SAVINGS AND LOAN ASSOCIATION,
Appellant,

vs.

NINI MYRNA TAN, *et al.*,
Appellees.

CALIFORNIA FEDERAL SAVINGS AND LOAN ASSOCIATION,
Appellant,

vs.

WILLIAM ROMAGNOLI, *et al.*, (and Consolidated Cases),
Appellees.

On Appeal from the California Court of Appeal, Fourth Appellate District.

MOTION TO AFFIRM OR DISMISS.

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Questions Presented.

The determination of appellees' Motion to Affirm or Dismiss depends upon a determination of the following issues:

1. By including a clause in its deed of trust stating that the contract is governed by the law of jurisdiction in which the property is located or is governed by the law of California, whether California Federal has thereby agreed to follow California law prohibiting unreasonable restraints on alienation, when the federal law commits the inclusion and enforcement of due-on-sale clauses to the contract between the borrower and lender?
2. Whether the Home Owners' Loan Act of 1933 occupies a field including the areas of real property and mortgages which are of fundamental state concern traditionally governed exclusively by state law, thus precluding the application of California Civil Code §711 to federal associations?
3. Whether Civil Code §711 conflicts with the Home Owners' Loan Act of 1933, or with regulations promulgated thereunder, to such a degree as to preclude its application to federal associations?

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Appellees.

MOTION TO AFFIRM OR DISMISS.

Statement of the Case.

In general, appellees have no quarrel with appellant's Statement of the Case. However, because 12 C.F.R. §545.6.11 (f) (now codified at 12 C.F.R. §545.8-3 (f)) by its own terms became effective July 31, 1976, the execution dates of the deeds of trust at issue here are relevant. The trust deeds at issue in the *Tan, Romagnoli* and *Dunn* cases were executed prior to the effective date of 12 C.F.R. §545.6-11 (f) (hereinafter all references will be 12 C.F.R. §545.8-3 (f) and (g)).

In addition, Appellants fail to point out that every trust deed at issue in this appeal contains a provision stating that the trust deed is governed by California Law. The trust deed in the Hanlon case contains the following provision:

> "15. Uniform Deed of Trust; Governing Law; Severability. This form of deed of trust combines uniform covenants for national use and non-uniform covenants with limited variations by jurisdiction to constitute a uniform security instrument covering real property. This Deed of Trust shall be governed by the law of the jurisdiction in which the Property is located. In the event that any provision or clause of this Deed of Trust or the Note conflicts with applicable law, such conflict shall not affect other provisions of this Deed of Trust or the Note which can be given effect without the conflicting provision, and to this end the provisions of the Deed of Trust and the Note are declared to be severable."

The trust deeds in the remaining cases contain the following provisions:

> "15. LAW OF CALIFORNIA CONTROLLING: This Deed shall be construed according to the laws of the State of California."

I.
MOTION TO DISMISS.

A. The Judgment of the Court of Appeal Rests on an Independent Non-Federal Basis in That the Court of Appeal Found That Appellant Contracted to Follow California Law Prohibiting Restraints on Alienation.

The Court of Appeal held that by the inclusion of paragraph 15 in its trust deeds, California Federal Savings and Loan Association ("Cal Fed") expressed an unmistakable intent to follow California law governing restraints on

alienation. *de la Cuesta v. Fidelity Federal Savings and Loan Association*, 121 Cal.App.3d 328, 342; 175 Cal.Rptr. 467 (1981).[1] Even if this Court agrees that Civil Code §711 is preempted, the Court of Appeal's judgment must nevertheless stand since it rests on an adequate non-federal basis.

Even if appellants correctly assert that federal law preempts, this means no more than state law does not apply of its own force. It does not necessarily mean that it is a violation of federal law for a federal association to contract to follow state law. Indeed, it is indisputable that under federal law a federal association can contract to enforce the due-on-sale clause only when its security interest is impaired. Thus, the question decided by the Court of Appeal was whether paragraph 15 had this effect.[2]

The Court of Appeal's construction of paragraph 15, contained in a local contract according to local law, is conclusive and does not raise a substantial federal question. *Black v. Cutter Laboratories*, 351 U.S. 292, 299 (1956). This Court will "examine the contract only to make certain that the non-federal ground of decision is not so colorable or unsubstantial as to be in effect an evasion of the constitutional issue." *Memphis Natural Gas Co. v. Beeler*, 315 U.S. 649, 654 (1941).

The Court of Appeal's interpretation of the effect of paragraph 15 is not bizarre and provides a substantial basis for

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[1]Inasmuch as the Court of Appeal's decision in the cases which are the subject of this appeal was based upon its own decision in *de la Cuesta*, all references will be to the *de la Cuesta* opinions. An appeal to this Court from the *de la Cuesta* decision, is currently pending. [*Fidelity Federal Savings and Loan Ass'n., et al. v. Reginald D. de la Cuesta, et al.*, No. 81-750].

[2]As applied to the due-on-sale clause, paragraph 15 is not a true choice-of-law provision, but merely a device for incorporating extrinsic material by reference. See, Restatement (Second) Conflicts of Law, §187, comment c.

its decision. Similar results have been reached even in cases where the federal fisc was directly involved. See *e.g.*, *United States v. Yazell*, 382 U.S. 341 (1966) and *United States v. Stewart*, 523 F.2d 1070 (9th Cir. 1975). The Court of Appeal applied the well established rule of construction that ambiguities are construed against the drafter, a rule which is applied as matter of federal law, *Bituminous Casualty Corp. v. Lynn*, 503 F.2d 636, 640-641 (6th Cir. 1974), even when the drafter is the United States. *Kenneth Reed Construction Corporation v. United States*, 475 F.2d 583, 587 (Ct. Cl. 1973); *Firestone Tire and Rubber Co. v. United States*, 444 F.2d 547, 551 (Ct. Cl. 1971).

II.
MOTION TO AFFIRM.

A. California Law Is Not Preempted by the Home Owners' Loan Act of 1933.

1. Since California's Prohibition of Unreasonable Restraints on Alienation Regulates an Area of Traditionally Local Concern, It Will Not Be Superseded Unless That Was the Clear and Manifest Purpose of Congress.

Whether a federal enactment preempts state law presents a question of congressional intent. *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977). State regulation in areas traditionally subject to local control[3] will not be precluded by a federal enactment "unless that was the clear and manifest purpose of Congress." *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1946).

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[3]In a long line of cases this Court has recognized that as a general rule, the areas of real property and mortgage law are governed by state law. See *e.g. Butner v. United States*, 440 U.S. 48, 55 (1979); *State Land Bd. v. Corvallis Sand & Gravel Co.*, 429 U.S. 353, 378 (1977); *United States v. Little Lake Misere Land Co.*, 412 U.S. 580, 591, 592 (1973); *Hoopeston Canning Co. v. Cullen*, 218 U.S. 313, 318 (1942); *Sunderland v. United States*, 266 U.S. 226, 233 (1924).

In recent years this Court has repeatedly emphasized that preemption of state law is not favored "in the absence of persuasive reasons — either the nature of the regulated subject matter permits no other conclusion or that the Congress has unmistakably so ordained." *Florida Lime and Avocado Growers v. Paul*, 373 U.S. 132, 147 (1963); *De Canas v. Bica*, 424 U.S. 351, 356 (1976); *Chicago and Northwestern Transportation Co. v. Kalo Brick and Tile Co.* 450 U.S. 311, 317 (1981); *Alessi v. Raybestos-Manhattan, Inc.*, ... U.S. ...., ... (1981); *Commonwealth Edison Co. v. Montana*, ... U.S. ...., ... (1981).

Even if Congress has the power to preclude the application of any state law whatsoever to federal associations, there is no rule which compels Congress to occupy the whole field. *Kelly v. Washington*, 302 U.S. 1 (1937).

> The [preemption] doctrine does not and could not in our federal system withdraw from the States either the "power to regulate where the activity regulated [is] a merely peripheral concern" of federal law (citation omitted), or the authority to legislate when Congress could have regulated "a distinctive part of a subject which is peculiarly adapted to local regulation . . . but did not," (citation omitted). *Chicago and Northwestern Transportation Co. v. Kalo Brick and Tile Co., supra*, 450 U.S. at 317.

This reluctance to find a total ouster of state authority "comports with the basic conception of federal law as interstitial in nature." Tribe, *American Constitutional Law*, 384, n.1 (1978).[4]

In addition, this reluctance to find a total ouster of state law preserves the state-federal balance from unintentional

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[4]See also Hart & Wechsler, *The Federal Courts and The Federal System* 470-471 (2nd Ed. 1973).

disturbance by Congress and unnecessary disturbance by the courts. *Jones v. Rath Packing Co., supra,* 430 U.S. at 525.[5] It is not a reflection of "doctrinaire localism," but is a reflection of the "presuppositions of our embracing federal system." *San Diego Building Trades Council v. Garmon,* 359 U.S. 236, 243 (1959).

2. Congress Did Not Express a Clear and Manifest Purpose to Preclude the Application of State Real Property and Mortgage Law to Federal Associations.

In support of the claim that Congress intended the HOLA to supersede state real property and mortgage law, appellants rely on the broad power granted to the Federal Home Loan Bank Board[6] ("Bank Board") and the comprehensive character of federal regulations. This Court has rejected the contention that the requisite congressional intent may be inferred merely from the comprehensive character of the federal program. *New York State Department of Social Services v. Dublino,* 413 U.S. 405, 415 (1973); *De Canas v. Bica, supra,* 424 U.S. at 359-360 (1976).

Even if an intent to preempt may be inferred solely from a comprehensive federal scheme, this does not necessarily mean that the field preempted is coterminous with the area in which the Bank Board may regulate. The mere fact that Congress granted the Bank Board authority to "regulate" federal associations does not indicate that Congress intended to prohibit the application of any state law to federal as-

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[5] "[T]he state is powerless to remove the ill effects of our decision, while the national government, which has the ultimate power, remains free to remove the burden." *Penn Dairies, Inc. v. Milk Control Commission,* 318 U.S. 261, 275 (1943).

[6] "In order to provide local mutual thrift institutions . . . the Board is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation, and regulation of associations to be known as 'Federal Savings and Loan Associations', . . ." 12 U.S.C. §1464 (a) (1).

sociations. *Cf., Ray v. Atlantic Richfield Co.*, 435 U.S. 151, 168-169 (1978). Thus, even if the HOLA is broad enough to permit the Bank Board to regulate in the areas of real property and mortgages, this does not mean that Congress intended the Bank Board's authority in these areas to be exclusive.

The existence of a comprehensive scheme should not and does not serve as a litmus paper test of preemption. In this case, several factors indicate that a comprehensive scheme does not imply a congressional intent to preempt. California Civil Code §711 is a substantive rule of real property — an area traditionally governed by state law. Additionally, it is not aimed at associations or even at financial institutions; it is a statute of general applicability. Because it is a statute of general applicability, it is not "regulation" of federal associations. *Cf., New York Telephone Co. v. New York State Department of Labor*, 440 U.S. 519, 532, 533 (1979).

It should also be noted that the Bank Board has not even attempted to regulate in the areas of real property and mortgages. The Bank Board has not regulated recording requirements, foreclosure proceedings, deficiency judgments, lien priorities, rights of redemption and the like. As the Court of Appeal pointed out, federal associations have always been governed by state real property and mortgage law. *de la Cuesta v. Fidelity Federal Savings and Loan Association, supra*, 121 Cal.App.3d at 337. The HOLA and the regulations promulgated thereunder, far from being comprehensive, are nonexistent in the areas of real property and mortgages.

The Court of Appeal determined that Congress did not intend to preclude the application of state law to the "external" affairs of a federal association, but recognized the Bank Board's plenary authority to "regulate" the "inter-

nal'' affairs of federal associations, *Id.* at 336-337, 340-341. Appellants have not cited, nor have appellees discovered, a single decision rejecting the internal/external distinction.[7] On the contrary, at least two Circuit Courts of Appeal have embraced the distinction. Federal law exclusively governs only the internal management of federal associations. *Gulf Federal Savings and Loan Association v. Federal Home Loan Bank Board,* 651 F.2d 259, 266 (5th Cir. 1981); *Murphy v. Colonial Federal Savings and Loan Association,* 388 F.2d 609, 612 (2nd Cir. 1967). Several district courts have also recognized the internal/external distinction. See *De Simone v. Warwick Federal Savings and Loan Association,* 482 F.Supp. 1190, 1194 (D.R.I. 1980); *City Federal Savings and Loan Association v. Crowley,* 393 F.Supp. 644, 655-656 (E.D. Wis. 1975); *Rettig v. Arlington Heights Federal Savings and Loan Association,* 405 F.Supp. 819, 823 (N.D. Ill. 1975).

While it is true that many courts have parroted the language of the court in *People v. Coast Federal Savings and Loan Association,* 98 F.Supp. 311 (S.D. Cal. 1951), that ''[T]he Board has adopted comprehensive rules and regulations concerning the powers of every federal savings and loan association from its cradle to its corporate grave'' (*Id.*

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[7]The decision in *Conference of Federal Savings and Loan Associations v. Stein,* 604 F.2d 1256 (9th Cir. 1979) aff'd., 445 U.S. 921 (1980) does not reject the internal/external distinction. The court divided the state provisions into two categories:

(1) those provisions conferring substantive rights on borrowers and

(2) those providing ''regulatory control'' over lenders. *Id.* at 1260. The court expressly declined to decide whether the first category of state laws was preempted. *Id.* Obviously this Court did not affirm a holding that the Circuit Court did not make. This Court's summary affirmance cannot be viewed as a rejection of the internal/external distinction. The statutes involved in *Stein* governed the internal affairs of the association.

at 316), it is a mistake to read this language literally. As this Court observed in *San Diego Building Trades Council v. Garmon, supra:*

> In the course of a process of tentative, fragmentary illumination carried on over more than a decade during which the writers of opinions almost inevitably, because unconsciously, focus their primary attention on the facts of particular situations, language may have been used or views implied which do not completely harmonize with the clear pattern which the decisions have evolved. *Id.* at 244.

The Court of Appeal in the within cases recognized the "clear pattern." While many cases contain broad statements of the preemptive effect of the HOLA, the courts in those cases were not faced with a question of state real property or mortgage law. Those cases dealt instead with such diverse issues as control over the establishment of branch offices, *North Arlington National Bank v. Kearny Federal Savings and Loan Association*, 187 F.2d 564 (3rd Cir. 1951) *cert. denied* 342 U.S. 816 (1951); *Lyons Savings and Loan Association v. Federal Home Loan Bank Board*, 377 F.Supp. 11 (N.D. Ill. 1974); the means of communication between the members of an association, *Kupiec v. Republic Federal Savings and Loan Association*, 512 F.2d 147 (7th Cir. 1975); and the use of mobile savings and loan facilities, *Central Savings and Loan Association of Chariton v. Federal Home Loan Bank Board*, 422 F.2d 504 (8th Cir. 1970).

The Court of Appeal's internal/external distinction demonstrates the proper "respect for the separate spheres of governmental authority preserved in our federalist system." *Alessi v. Raybestos-Manhattan, Inc., supra,* .... U.S. at .... . State real property and mortgage law has ancient roots and has evolved over time into an intricate and interrelated body of law carefully balancing competing and conflicting

interests and goals. The mere fact that Congress granted the Bank Board broad power to regulate federal associations is not sufficient evidence of a "clear and manifest purpose of Congress" to sweep all this away. Regulation of restraints on alienation is at best only a peripheral concern of the HOLA. It is not within the central aim of the HOLA; it is peculiarly adapted to local regulation.

B. California's Prohibition of Restraints on Alienation Does Not Conflict With Any Regulation Promulgated by the Bank Board.

1. Occupation of the Field by Administrative Fiat Has Never Been Sustained.

Absent congressional intent to supersede even harmonious state law, state law is superseded only to the extent that it actually conflicts with a federal statute. *Katherine Gibbs, Inc. v. F.T.C.*, 612 F.2d 658, 666-667 (2d Cir. 1979). A federal agency may not, under the guise of interpretation, expand or restrict the operation of a federal statute. See *e.g., United States v. Colamaro*, 354 U.S. 351 (1957); *Neuberger v. Commissioner*, 311 U.S. 83 (1940); *Texas & Pacific Railroad Co. v. U.S.*, 289 U.S. 627 (1933).

If Congress intends to exclude even harmonious state regulation, any attempt by a federal agency to accomplish this same goal is superfluous. If Congress does not intend to exclude even harmonious state regulations, any attempt by a federal agency to do so is beyond its power. The Court of Appeal correctly observed the difference between regulatory agency enactments and the necessary Congressional intent to preempt;

> The decision whether to displace state law is a fundamental one going to the very fabric of federalism; thus, the decision is one to be made by the people through their elected representatives in Congress rather

> than by agencies or tribunals insulated from democratic pressures. (Citations omitted.) *de la Cuesta v. Fidelity Federal Savings and Loan Association, supra,* 121 Cal.App.3d at 339-340.

Thus, the Bank Board's regulations can have no greater preemptive effect than that which would normally follow from inconsistency or repugnancy.

Appellants suggest that if the Bank Board intends preemption, preemption occurs even in the absence of conflict between state and federal law. This suggestion is totally without support.

On many occasions this Court has held that in the absence of a Congressional intent to preclude the application of state law, state law is void only to the extent that it actually conflicts with a federal enactment. See *e.g. Ray v. Atlantic Richfield, supra,* 435 U.S. at 158. This Court has never suggested that a federal agency could preclude the application of harmonious state law when Congress did not so intend.

This Court's decision in *United States v. Shimer,* 367 U.S. 374 (1961) does not hold to the contrary. This Court phrased the question presented as whether "the application of state law to determine the Administration's obligation to Excelsior is inconsistent with the Regulations prescribed by the agency charged with administering the Servicemen's Readjustment Act." (Emphasis added). *Id.* at 377. This Court was not presented with the question whether the application of state law consistent with federal regulations was permissible.

2. The Application of California Civil Code §711 to Federal Associations Does Not Conflict With 12 C.F.R. §545.8-3 (f) and (g).

As a preliminary matter, 12 C.F.R. §545.8-3 (f) is not applicable to the *Tan, Romagnoli* or *Dunn* deeds of trust. By its own terms this regulation was not effective until July

31, 1976. (See Federal Home Loan Bank Board Resolution 76-296.) Since each of the deeds of trust in the *Tan, Romagnoli* and *Dunn* cases were executed prior to this date, 12 C.F.R. §545.8-3 (f) and (g) have no application to these cases.

In any event, the Court of Appeal correctly followed the controlling precedent in determining that Civil Code §711 does not conflict with the due-on-sale regulation. The Court of Appeal concluded that there was no conflict since it is possible for federal associations to comply with both state and federal law, relying on this Court's decision in *Florida Lime and Avocado Growers, Inc. v. Paul, supra.*

In a recent case the Ninth Circuit employed reasoning analogous to that of the Court of Appeal. In *Credit Data of Arizona, Inc. v. State of Arizona,* 602 F.2d 195 (9th Cir. 1979), the court upheld the application of a state law prohibiting a credit agency from imposing a fee for disclosing its sources of credit information, even though the federal Fair Credit Reporting Act explicitly permitted such a charge. *Id.* at 198. In reaching this result, the court relied upon this Court's reasoning in *Jones v. Rath Packing, supra, Id.* In *Jones,* this Court reasoned that a state statute is not inconsistent with a federal enactment when it is possible to comply with both the state and federal rules without triggering federal enforcement action. *Jones v. Rath Packing, supra,* 430 U.S. at 540.

In *Goldstein v. California,* 412 U.S. 546 (1973), this Court held that state legislation, to be preempted, must be "absolutely and totally contradictory and repugnant." *Id.* at 533. Civil Code §711 cannot be characterized as such. This is especially true given the language of the Bank Board's due-on-sale regulation. That regulation authorizes the inclusion and enforcement of a due-on-sale clause as a matter of contract.

In *De Simone v. Warwick Federal Savings and Loan Association, supra,* the court construed 12 C.F.R. §545.6-11 (d) (now codified at 12 C.F.R. §545.8-3 (d)), governing the imposition of late charges. This regulation contains a form of language identical to that in the due-on-sale regulation, and provides that an association may include a late charge provision in its loan instrument "as a matter of contract" and that the "assessment, imposition and collection of a late charge shall be exclusively governed by the terms of the contract." The court concluded that the regulation "seems to indicate a strong intent to leave late charges to the contract, and not to detailed federal supervision." *Id.*, 482 F.Supp. at 1193. The court further held that any violation of the terms of the contract by the association would not constitute a regulatory violation. *Id.* at 1194.

Similarly, the due-on-sale regulation leaves due-on-sale clauses to the contract and not to detailed federal supervision. Commercial agreements are traditionally governed by the states. *Aronson v. Quick Point Pencil Co.*, 440 U.S. 257 (1979). The "invalidation of contract clauses held repugnant to state public policy is a proper exercise of the state judicial function." *Mariniella v. Shell Oil Company,* 511 F.2d 853, 858 (3rd Cir. 1975). Since the due-on-sale regulation merely permits the inclusion and enforcement of a due-on-sale clause in a federal association's loan documents as a matter of contract, California's prohibition of its use when it restrains the alienation of property does not constitute an "actual conflict between the two schemes that they both cannot stand in the same area." *Florida Lime and Avocado Growers v. Paul, supra,* 373 U.S. at 141.

The mere fact that federal law permits the use of a due-on-sale clause does not necessarily mean that any state law which places limitations on its use is invalid. This Court

has upheld the application to national banks of a state statute prohibiting the use of real property as security for a pre-existing debt, even though federal law specifically allowed national banks to use real property as security for pre-existing debts. *McClellan v. Chipman*, 164 U.S. 347 (1896) *Cf., Huron Portland Cement Co. v. Detroit*, 362 U.S. 440, 444-447 (1960).

C. Retrospective Application of Wellenkamp Does Not Result in an Unconstitutional Impairment of Contractual Obligation.

Appellants' contention that the retrospective application of *Wellenkamp v. Bank of America*, 21 Cal.3d 943, 148 Cal.Rptr. 379 (1978) violates the contract clause of the United States constitution is without merit. The contract clause does not apply to judicial decisions, but only t legislative action. *Tidal Oil Co. v. Flanagan*, 263 U.S. 444, 450-451 (1923); *Allied Structural Steel Co. v. Spannus*, 438 U.S. 234, 257 (1978) (dissenting opinion). Indeed this Court in *Tidal Oil* held that this question has been answered so many times that it presents no federal question. *Id.* at 451-452.

Conclusion.

The prior cases on preemption clearly indicate that the mere delegation of power to the Bank Board to "regulate" federal associations is not sufficient to preclude the application of state real property and mortgage law to federal associations. Furthermore, appellants have failed to present a substantial claim that California Civil Code §711 conflicts with the federal scheme.

Even if this Court disagrees, and believes that these issues deserve plenary consideration, the appeal in this case should be dismissed because the judgment of the Court of Appeal rests on an adequate non-federal basis.

Respectfully submitted,

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